

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended. Filing is mandatory.

Local Government Type: <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name: <u>Three Rivers Health</u>	County St. Joseph
Audit Date December 31, 2005	Opinion Date February 16, 2006	Date Accountant Report Submitted To State: March 23, 2006	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:


1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations.

You must check the applicable box for each item below:

- | | |
|---|---|
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements. |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980). |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended). |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act. |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91] or P.A. 55 of 1982, as amended [MCL 38.1132]) |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit. |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241). |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95). |

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Reports on individual federal assistance programs (program audits).	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Single Audit Reports (ASLGU).	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>

Certified Public Accountant (Firm Name): PLANTE & MORAN, PLLC			
Street Address 750 Trade Centre Way, Suite 300	City Portage	State MI	ZIP 49002
Accountant Signature 			

Three Rivers Health

Consolidated Financial Report December 31, 2005

Three Rivers Health

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Independent Auditor's Report

To the Board of Directors
Three Rivers Health

We have audited the accompanying consolidated balance sheet of Three Rivers Health as of December 31, 2005 and 2004 and the related consolidated statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Three Rivers Health at December 31, 2005 and 2004 and the consolidated results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements do not present a management's discussion and analysis, which would be an analysis of the financial performance for the year. The Governmental Accounting Standards Board has determined that this analysis is necessary to supplement, although not required to be a part of, the basic financial statements.

Plante & Moran, PLLC

February 16, 2006

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Three Rivers Health

Consolidated Balance Sheet

	December 31, 2005	December 31, 2004
Assets		
Current Assets		
Cash and cash equivalents (Note 2)	\$ 2,126,403	\$ 1,320,189
Accounts receivable (Note 3)	4,763,458	4,661,222
Assets limited as to use (Note 2)	147,412	130,334
Other current assets	949,845	1,028,621
Total current assets	7,987,118	7,140,366
Assets Limited as to Use (Note 2)	2,696,156	5,852,558
Property and Equipment (Note 4)	17,478,715	14,042,899
Total assets	\$ 28,161,989	\$ 27,035,823
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt (Note 6)	\$ 1,307,045	\$ 1,179,946
Accounts payable	2,417,110	1,352,680
Estimated third-party payor settlements (Note 5)	532,000	1,100,000
Accrued liabilities and other:		
Accrued compensation	432,728	154,477
Accrued compensated absences	910,344	805,969
Construction payable	142,286	243,057
Other accrued liabilities	392,839	351,663
Total current liabilities	6,134,352	5,187,792
Long-term Debt (Note 6)	10,082,873	11,149,591
Total liabilities	16,217,225	16,337,383
Net Assets		
Invested in capital assets - Net of related debt	6,088,797	1,713,362
Restricted:		
Restricted for debt service	147,412	130,334
Restricted for capital acquisitions	226,940	2,290,625
Unrestricted	5,481,615	6,564,119
Total net assets	11,944,764	10,698,440
Total liabilities and net assets	\$ 28,161,989	\$ 27,035,823

Three Rivers Health

Consolidated Statement of Revenues, Expenses, and Changes in Net Assets

	Year Ended	
	December 31, 2005	December 31, 2004
Operating Revenues		
Net patient service revenue	\$ 40,475,803	\$ 37,969,979
Other	1,257,920	458,618
Total operating revenues	41,733,723	38,428,597
Operating Expenses		
Salaries and wages	15,908,844	14,827,298
Employee benefits and payroll taxes	4,886,500	4,456,901
Operating supplies and expenses	4,365,815	4,007,270
Professional services and consultant fees	4,469,366	3,840,058
Purchased services	4,634,198	4,804,663
Professional liability costs	1,338,873	1,404,372
Utilities	513,942	455,999
Repairs and rentals	886,785	752,633
Other	1,327,352	770,912
Depreciation and amortization	1,845,113	1,844,991
Total operating expenses	40,176,788	37,165,097
Operating Income	1,556,935	1,263,500
Nonoperating Revenue (Expense)		
Interest income	67,708	67,464
Contributions	77,621	72,013
Interest expense	(455,940)	(532,721)
Total nonoperating expense	(310,611)	(393,244)
Increase in Net Assets	1,246,324	870,256
Net Assets - Beginning of year	10,698,440	9,828,184
Net Assets - End of year	\$ 11,944,764	\$ 10,698,440

Three Rivers Health

Consolidated Statement of Cash Flows

	Year Ended	
	December 31, 2005	December 31, 2004
Cash Flows from Operating and Nonoperating Activities		
Cash received from patients and third-party payors	\$ 39,323,010	\$ 37,421,020
Cash payments to employees and suppliers	(36,516,258)	(34,663,810)
Other receipts from operations	1,257,920	458,618
Net cash provided by operating and nonoperating activities	4,064,672	3,215,828
Cash Flows from Noncapital Financing Activities - Donations	77,621	72,013
Cash Flows from Investing Activities		
Investment income	67,708	67,464
Increase (decrease) in assets limited as to use	(489,547)	334,995
Net cash (used in) provided by investing activities	(421,839)	402,459
Cash Flows from Capital and Related Financing Activities		
Acquisition and construction of capital assets	(4,871,644)	(1,836,053)
Proceeds from sale of capital assets	1,450	-
Issuance of long-term debt	-	4,100,000
Interest paid on long-term debt	(455,940)	(532,721)
Principal payments on long-term debt	(1,216,977)	(2,464,096)
Net cash used in capital and related financing activities	(6,543,111)	(732,870)
Net (Decrease) Increase in Cash and Cash Equivalents	(2,822,657)	2,957,430
Cash and Cash Equivalents - Beginning of year	5,629,938	2,672,508
Cash and Cash Equivalents - End of year	\$ 2,807,281	\$ 5,629,938
Balance Sheet Classification for Cash		
Current assets	\$ 2,126,403	\$ 1,320,189
Assets limited as to use	680,878	4,309,749
Total cash	\$ 2,807,281	\$ 5,629,938

Three Rivers Health

Consolidated Statement of Cash Flows (Continued)

A reconciliation of operating income to net cash from operating activities is as follows:

	Year Ended	
	December 31, 2005	December 31, 2004
Cash Flows from Operating Activities		
Operating income	\$ 1,556,935	\$ 1,263,500
Adjustments to reconcile operating income to net cash from operating activities:		
Depreciation	1,845,113	1,844,993
Provision for bad debts	3,672,359	2,974,770
Loss on disposal of capital assets	8,909	-
Changes in assets and liabilities:		
Increase in patient accounts receivable	(4,825,152)	(3,573,730)
(Increase) decrease in other current assets	78,776	(268,246)
Increase in accounts payable	922,144	659,800
Increase in other accrued expenses	323,031	264,741
Increase in third-party settlement payables	482,557	50,000
Net cash provided by operating activities	<u><u>\$ 4,064,672</u></u>	<u><u>\$ 3,215,828</u></u>

Significant noncash investing, capital, and financing activities for 2005 and 2004 are as follows:

In 2005 and 2004, the Hospital leased equipment under capital leases. These obligations were for \$277,358 and \$161,711 in 2005 and 2004, respectively.

In 2005 and 2004, the Hospital had \$142,286 and \$243,057 due on a construction payable for assets included in property and equipment in 2005 and 2004, respectively.

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 1 - Nature of Business and Significant Accounting Policies

Three Rivers Health (the "Hospital") is a governmental unit that operates a short-term acute care facility providing inpatient and outpatient health care services to the Three Rivers, Michigan area. TRAH Properties, a wholly owned subsidiary of the Hospital, leases space to the Hospital for services provided to its patients. Integrated Health Systems (IHS), a wholly owned subsidiary of the Hospital, employs physicians who work at the Hospital as contracted employees. Physicians Health Organization (PHO) is a joint venture between the Hospital and local physicians to provide computer services, as well as a 50-50 risk share pool to doctors who refer patients to the Hospital. The Hospital also has established a foundation, whose purpose is to obtain funds to directly benefit the Hospital.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Basis of Presentation - The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, issued in June 1999. The Hospital follows the "business-type" activities reporting requirements of GASB Statement No. 34 that provide a comprehensive look at the Hospital's financial activities. No component units are required to be reported in the Hospital's financial statements.

Enterprise Fund Accounting - The Hospital uses Enterprise Fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Fund Accounting*, as amended, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

Affiliated Organization - The Hospital has a formal agreement with a local health care provider whereby both organizations will work toward the mutual benefit of one another in furtherance of promoting an integrated health care delivery system in southwest Michigan. The Hospital has available the technical and financial resources of its affiliate and participates in the affiliate's sponsored managed care programs. This affiliation agreement terminates October 31, 2008.

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note I - Nature of Business and Significant Accounting Policies (Continued)

Assets Limited as to Use - Assets limited as to use include assets set aside by the board of trustees for future capital improvements over which the board retains control and may at its discretion subsequently use for other purposes and assets temporarily restricted under terms of a bond agreement for future bond payments and capital projects.

Investments - Investments are carried at fair value.

Property and Equipment - Property and equipment are stated at cost. Maintenance and repairs are charged to expense as incurred. Depreciation has been charged to operations using the straight-line method and includes amortization of capital leases.

Paid Time Off - The Hospital maintains a paid time off benefit policy. The benefits are charged to operations when earned. Unused benefits are recorded as a current liability in the consolidated financial statements.

Classification of Net Assets - Net assets of the Hospital are classified in three components. Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted net assets are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital, including amounts deposited with trustees as required by revenue bond indentures. Unrestricted net assets are remaining net assets that do not meet the definition of the other two categories of net assets. Included in the unrestricted net assets reported at December 31, 2005 and 2004 is \$2,469,216 and \$3,561,933, respectively, which has been designated by the Hospital's board of trustees for future capital acquisitions. Designated funds remain under the control of the board of trustees, which may at its discretion later use the funds for other purposes.

Net Patient Service Revenue - The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactively calculated adjustments arising under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Management believes that it is in compliance with all applicable laws and regulations. Final determination of compliance of such laws and regulations is subject to future government review and interpretation. Violations may result in significant regulatory action including fines, penalties, and exclusions from the Medicare and Medicaid programs.

Charity Care - The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Charity care was less than 1 percent of gross charges for the years ended December 31, 2005 and 2004.

Operating Revenue and Expenses - The Hospital's statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services - the Hospital's principal activity. Operating expenses are all expenses incurred to provide health care services, other than financing costs. Nonoperating activities, including investment income and contributions received for purposes other than capital asset acquisition, and interest expense, are reported as nonoperating revenue and expense.

Tax Status - The Hospital and TRAH Properties are not-for-profit corporations as described in Section 501(c)(3) of the Internal Revenue Code and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. IHS is deemed a corporation and files an 1120, with no tax due, and PHO files a 1065 partnership return.

Note 2 - Deposits and Investments

Michigan Compiled Laws Section 129.91 (Public Act 20 of 1943, as amended) authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated within the two highest classifications, which matures not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions, which are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 2 - Deposits and Investments (Continued)

The Hospital has adopted an investment policy that follows Public Act 20 of 1943, as amended.

The Hospital's cash and investments are subject to several types of risk, which are examined in more detail below:

Custodial Credit Risk of Bank Deposits - Custodial credit risk is the risk that in the event of a bank failure, the Hospital's deposits may not be returned to it. The Hospital does not have a deposit policy for custodial credit risk. At December 31, 2005 and 2004, the Hospital had deposits of \$3,283,602 and \$3,371,257, respectively, of bank deposits (checking, savings, and money market accounts) of which \$400,000 and \$300,000, respectively, were covered by FDIC insurance. The Hospital believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the Hospital evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Concentration of Credit Risk - The Hospital places no limit on the amount the Hospital may invest in any one type of investment.

The detail of assets limited as to use, consisting of cash and investments in government-backed securities, is summarized in the following schedule:

	2005	2004
Restricted under the terms of the bond agreement for debt service	\$ 147,412	\$ 130,334
Restricted under the terms of the bond agreement for capital expansion project	226,940	2,290,625
Designated by board for future capital acquisitions	2,469,216	3,561,933
Total assets limited as to use	2,843,568	5,982,892
Less current portion	147,412	130,334
Total long-term assets limited as to use	\$ 2,696,156	\$ 5,852,558

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 3 - Patient Accounts Receivable

The details of patient accounts receivable are set forth below:

	2005	2004
Patient accounts receivable	\$ 10,715,458	\$ 10,725,222
Less:		
Allowance for uncollectible accounts	(1,589,000)	(1,387,000)
Allowance for contractual adjustments	(4,363,000)	(4,677,000)
Net patient accounts receivable	<u>\$ 4,763,458</u>	<u>\$ 4,661,222</u>
	Percentage	
Medicare	28	24
Blue Cross Blue Shield of Michigan	15	15
Medicaid	15	14
Commercial insurance and HMOs	25	27
Self-pay	17	20
Total	<u>100</u>	<u>-</u>

Note 4 - Capital Assets

Cost of capital assets and related depreciable lives for December 31, 2005 are summarized below:

	2004	Additions	Transfers	Retirements	2005	Depreciable Life - Years
Land	\$ 219,500	\$ -	\$ -	\$ -	\$ 219,500	
Land and land improvements	1,023,833	1,788	-	(10,359)	1,015,262	5-25
Buildings and improvements	13,018,644	610,619	-	-	13,629,263	10-40
Furniture, fixtures, and equipment	17,467,209	937,803	121,550	-	18,526,562	3-20
Buildings and equipment under capital lease	3,499,107	279,064	(121,550)	-	3,656,621	3-40
Construction in progress	1,194,816	3,462,014	-	-	4,656,830	
Total	<u>36,423,109</u>	<u>5,291,288</u>	<u>-</u>	<u>(10,359)</u>	<u>41,704,038</u>	
Less accumulated depreciation:						
Land and land improvements	706,790	38,418	-	-	745,208	
Buildings and improvements	6,134,931	704,680	-	-	6,839,611	
Furniture, fixtures, and equipment	14,835,839	1,048,052	-	-	15,883,891	
Buildings and equipment under capital lease	702,650	53,963	-	-	756,613	
Total	<u>22,380,210</u>	<u>1,845,113</u>	<u>-</u>	<u>-</u>	<u>24,225,323</u>	
Net carrying amount	<u>\$ 14,042,899</u>	<u>\$ 3,446,175</u>	<u>\$ -</u>	<u>\$ (10,359)</u>	<u>\$ 17,478,715</u>	

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 4 - Capital Assets (Continued)

Cost of capital assets and related depreciable lives for December 31, 2004 are summarized below:

	2003	Additions	Transfers	Retirements	2004	Depreciable Life - Years
Land	\$ 219,500	\$ -	\$ -	\$ -	\$ 219,500	
Land and land improvements	903,382	120,451	-	-	1,023,833	5-25
Buildings and improvements	12,727,267	118,378	172,999	-	13,018,644	10-40
Furniture, fixtures, and equipment	16,046,223	645,462	775,524	-	17,467,209	3-20
Buildings and equipment under capital lease	4,285,919	161,711	(948,523)	-	3,499,107	3-40
Construction in progress	-	1,194,816	-	-	1,194,816	
Total	34,182,291	2,240,818	-	-	36,423,109	
Less accumulated depreciation:						
Land and land improvements	671,552	35,238	-	-	706,790	
Buildings and improvements	5,403,233	682,317	49,381	-	6,134,931	
Furniture, fixtures, and equipment	13,260,909	950,428	624,502	-	14,835,839	
Buildings and equipment under capital lease	1,199,525	177,008	(673,883)	-	702,650	
Total	20,535,219	1,844,991	-	-	22,380,210	
Net carrying amount	\$ 13,647,072	\$ 395,827	\$ -	\$ -	\$ 14,042,899	

At December 31, 2005, the Hospital had commitments related to renovations and expansion of the Urgent Care/Emergency Department and Testing Unit clinical space and the expansion and remodeling of other specific areas of the Hospital. The projected cost to complete these projects is \$525,000.

Note 5 - Cost Report Settlements

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Approximately 69 percent of the Hospital's net patient service revenue is received from the Medicare, Medicaid, and Blue Cross Blue Shield of Michigan programs. Subsidiaries of the Hospital have agreements with third-party payors that provide for reimbursement at amounts different from established rates. A summary of the basis of reimbursement with these third-party payors are as follows:

- **Medicare** - Inpatient, acute-care, and rehabilitation services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors. Inpatient rehabilitation services are reimbursed at cost subject to a per case limit. Outpatient services related to Medicare beneficiaries are reimbursed based on an established fee-for-service methodology.

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 5 - Cost Report Settlements (Continued)

- **Medicaid** - Inpatient, acute-care services rendered to Medicaid program beneficiaries are also paid at prospectively determined rates per discharge. Capital costs relating to Medicaid patients are paid on a cost-reimbursement method. Outpatient services are reimbursed on an established fee-for-service methodology.
- **Blue Cross Blue Shield of Michigan** - The Hospital is reimbursed its controlled charges for services provided to Blue Cross subscribers.

Laws and regulations governing the Medicare, Medicaid, and Blue Cross Blue Shield programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

Cost report settlements result from the adjustment of interim payments to final reimbursement under these programs and are subject to audit by fiscal intermediaries. Although these audits may result in some changes in these amounts, they are not expected to have a material effect on the accompanying consolidated financial statements.

Note 6 - Long-term Debt

Long-term liability activity for the year ended December 31, 2005 was as follows:

	2004	Current Year Additions	Current Year Reductions	2005	Amounts Due Within One Year
Series 1993	\$ 3,220,000	\$ -	\$ (545,000)	\$ 2,675,000	\$ 625,000
Series 1997	2,321,000	-	(250,000)	2,071,000	260,000
Series 2004	4,100,000	-	(166,966)	3,933,034	153,897
Lease payable to affiliate	2,402,867	-	(106,363)	2,296,504	112,810
Lease payable	285,670	277,358	(148,648)	414,380	155,338
Total long-term debt	<u>\$ 12,329,537</u>	<u>\$ 277,358</u>	<u>\$ (1,216,977)</u>	<u>\$ 11,389,918</u>	<u>\$ 1,307,045</u>

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 6 - Long-term Debt (Continued)

Long-term liability activity for the year ended December 31, 2004 was as follows:

	2003	Current Year Additions	Current Year Reductions	2004	Amounts Due Within One Year
Series 1993	\$ 3,745,000	\$ -	\$ (525,000)	\$ 3,220,000	\$ 545,000
Series 1997	2,551,000	-	(230,000)	2,321,000	250,000
Series 2003	1,437,000	-	(1,437,000)	-	-
Series 2004	-	4,100,000	-	4,100,000	166,966
Lease payable to affiliate	2,523,255	-	(120,388)	2,402,867	106,362
Lease payable	274,733	161,711	(150,774)	285,670	111,618
Total long-term debt	<u>\$ 10,530,988</u>	<u>\$ 4,261,711</u>	<u>\$ (2,463,162)</u>	<u>\$ 12,329,537</u>	<u>\$ 1,179,946</u>

The bonds payable are summarized as follows:

- Bonds payable - 1993 Series, total annual principal payments ranging from \$625,000 due in 2006 to \$715,000 due in 2009, collateralized by net revenue derived from the operations of the Hospital. The interest rate is 5.44 percent.
- Bonds payable - 1997 Series, total annual principal payments ranging from \$260,000 due in 2006 to \$370,000 due in 2011, with the last payment of \$201,000 scheduled to be made in May 2012, collateralized by net revenue derived from the operations of the Hospital. The interest rate is 5.59 percent.
- Bonds payable - 2004 Series, total annual principal payments ranging from \$153,897 due in 2006 to \$270,485 due in 2024. The debt is collateralized by the net revenue derived from the operations of the Hospital. The interest rate is 5.39 percent.
- Lease payable to an affiliate organization, monthly installments aggregating approximately \$20,500, including interest at 6.0 percent per annum, collateralized by two buildings
- Lease payable, monthly installments aggregating approximately \$13,000, including interest at 5.08 - 5.22 percent per annum, collateralized by equipment

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 6 - Long-term Debt (Continued)

The following is a schedule by years of bond principal and interest as of December 31, 2005:

Year Ending December 31	Long-term Debt		Capital Lease Obligation	
	Principal	Interest	Principal	Interest
2006	\$ 1,038,897	\$ 371,680	\$ 268,148	\$ 150,299
2007	1,093,797	316,863	273,858	135,244
2008	1,143,534	259,734	199,926	122,120
2009	1,204,059	199,756	166,066	111,199
2010	514,442	146,271	142,637	102,640
2011-2015	1,529,859	452,660	853,938	372,447
2016-2020	1,121,496	263,080	806,311	92,447
2021-2025	1,032,950	74,711	-	-
Total				
payments	\$ 8,679,034	\$ 2,084,755	\$ 2,710,884	\$ 1,086,396

Note 7 - Defined Contribution Pension Plan

The Hospital maintains a defined contribution retirement plan covering substantially all employees. The Hospital has recognized contribution expense totaling \$462,223 and \$451,214 during the years ended December 31, 2005 and 2004, respectively. Expense was determined in accordance with the plan formula as follows:

The Hospital will make fixed contributions of employees' W-2 wages for those employees who have completed their probationary period and are employed on either a full-time or part-time basis during the final pay period of each calendar year. The fixed contributions will be paid during the first quarter of each succeeding year. The fixed contribution rates are set forth as follows:

- Employees who have completed their probationary period up to 10 years of services - 2 percent employer contribution
- Employees who have completed 11 to 14 years of service - 3 percent employer contribution
- Employees who have completed 15 years of service and up - 4 percent employer contribution

In addition, the Hospital will make matching contributions equal to 50 percent of an employee's contributions, up to a maximum of 2 percent of the employee's compensation.

Three Rivers Health

Notes to Consolidated Financial Statements December 31, 2005 and 2004

Note 8 - Risk Management

The Hospital is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The Hospital has purchased commercial insurance for property loss, fraud, director and officer liability, professional liability, malpractice, general liability, employee medical, and workers' compensation claims.

The Hospital is insured against medical malpractice claims under a claims-made policy, whereby only the claims reported to the insurance carrier during the policy period are covered regardless of when the incident giving rise to the claim occurred. Under the terms of the policy, the Hospital bears the risk of the ultimate costs of any individual claim or aggregate claims exceeding claim limits asserted in the policy year. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during the claims-made term, but reported subsequently, will be uninsured.

There are several pending malpractice claims against the Hospital. There is insurance coverage, but it is possible that the liability for the claims may exceed the aggregate insurance coverage. Presently, it is not possible to determine the resolution of the claims or amount of liability, if any. Accruals for estimated deductibles are included in current liabilities at December 31, 2005 and 2004.